

**Letter of Findings Number: 07-0672**  
**Adjusted Gross Income Tax**  
**For the Tax Years 2003-2005**

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**ISSUES**

**I. Adjusted Gross Income Tax – Imposition.**

**Authority:** IC § 6-8.1-5-1(b); IC § 6-3-2-1(a); IC § 6-3-5-1; [45 IAC 3.1-1-115](#).

The Taxpayer protests the imposition of Indiana adjusted gross income tax.

**II. Tax Administration – Negligence Penalty.**

**Authority:** IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#)(b)(c).

The Taxpayer protests the imposition of the negligence penalty.

**STATEMENT OF FACTS**

The Taxpayer is an Ohio resident who received payment for work performed in Indiana. The Indiana Department of Revenue (Department) imposed adjusted gross income tax, interest, and penalty on the Taxpayer's Indiana income for the tax years 2003-2005. The Taxpayer protested the assessment. A telephone hearing was held and this Letter of Findings results.

**ISSUES**

**I. Adjusted Gross Income Tax – Imposition.**

**DISCUSSION**

The Department assessed adjusted gross income tax on the Taxpayer's earnings from work performed in Indiana pursuant to IC § 6-3-2-1(a). The Taxpayer protested this assessment. The Taxpayer contended that it reported the income in question on its Ohio adjusted gross income tax return and paid the resulting tax to Ohio pursuant to the reciprocity agreement between Indiana and Ohio.

The issue to be determined is whether the income from work performed in Indiana should have been reported and tax remitted to Indiana or Ohio.

All tax assessments are presumed to be valid. IC § 6-8.1-5-1(c). The Taxpayer bears the burden of proving that any assessment is incorrect. *Id.*

The law concerning the reporting of Indiana income of nonresidents who live in a state having a reciprocity agreement with Indiana is found at IC § 6-3-5-1 as follows:

The tax imposed by [IC 6-3-2](#) on the adjusted gross income derived from sources within the state of Indiana by persons who are nonresidents of this state, shall not be payable if the laws of the state or territory of residence of such persons, at the time such adjusted gross income was earned in this state, contained a reciprocal provision by which residents of this state were exempted from taxes imposed by such state on income earned in such state.

The provisions of the reciprocity agreement are stated in the Adjusted Gross Income Tax Regulations at [45 IAC 3.1-1-115](#) as follows:

Reciprocity agreements. Reciprocal income tax agreements now exist between Indiana and the states of Illinois, Kentucky, Michigan, Ohio, Pennsylvania and Wisconsin. The agreements provide that Indiana will not impose its adjusted gross income tax on salaries, wages and commissions earned by legal residents of these states in Indiana and they in turn will not impose their individual income tax on wages, salaries and commissions earned by legal residents of Indiana in those states.

The reciprocity agreement states that Ohio residents report and pay adjusted gross income tax on income earned for work performed in Indiana if the income was in the form of salaries, wages, or commissions. These forms of income would be reported on a W-2. In this case, the Taxpayer's income from activities performed in Indiana was reported on form 1099. This form is used when the person performing the work is an independent contractor, who is receiving nonemployee compensation. As an independent contractor, the Taxpayer did not receive a salary, wage, or commission for work performed in Indiana. Therefore, the adjusted gross income tax on the income the Taxpayer received for work performed in Indiana was properly reportable to Indiana. The Taxpayer owes Indiana adjusted gross income tax on the 1099 income resulting from work performed in Indiana pursuant to IC § 6-3-2-1(a).

Alternatively, the Taxpayer argues that it should not have to pay adjusted gross income tax to Indiana because it already paid adjusted gross income tax on the income at issue to Ohio. Those taxes were, however, remitted to Ohio in error. Therefore, the Taxpayer's proper remedy is to request a refund from Ohio of the taxes paid in error and pay Indiana adjusted gross income tax on the Taxpayer's 1099 income received for services performed in Indiana.

**FINDING**

The Taxpayer's protest is respectfully denied.

**II. Tax Administration - Ten Percent Negligence Penalty**

**DISCUSSION**

The Taxpayer protests the imposition of the ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Indiana Regulation [45 IAC 15-11-2](#)(b) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at [45 IAC 15-11-2](#)(c) as follows:

The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

The Taxpayer provided substantial documentation to indicate that its failure to pay the assessed adjusted gross income tax was due to reasonable cause rather than negligence.

**FINDING**

The Taxpayer's protest to the imposition of the penalty is sustained.

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